

## Memorandum

*Flex your power!  
Be energy efficient!*

**To:** BILL FACKENTHALL  
Chief  
Division of Procurement and Contracts

**Date:** June 30, 2010

**File:** P4000-0375

CLARK PAULSEN  
Chief  
Division of Accounting

**ORIGINAL SIGNED BY:**

**From:** GERALD A. LONG  
Deputy Director  
Audits and Investigations

**Subject:** Final Audit Report – Contract Delegation

Attached is Audits and Investigations' final audit report on the California Department of Transportation's (Department) Contract Delegation as required under the provisions of the Department of General Services (DGS) Exemption Letter No. 11.9, dated June 30, 2008. Your response has been included as part of our final report. This report is intended for your information and Department management. As a matter of public record, the report will be included on the Reporting Transparency in Government Web site.

Please provide our office with status reports on the implementation of your audit finding dispositions 60, 180, and 360 days subsequent to the report date. If all findings have not been corrected within 360 days, please continue to provide status reports every 180 days until the audit findings are fully resolved.

We thank you and your staff for their assistance provided during this audit. If you have any questions or need additional information, please call Laurine Bohamera, Chief, Internal Audits, at (916) 323-7107, or me at (916) 323-7122.

**Attachment**

c: Cindy McKim, Director  
Malcolm Dougherty, Interim Chief Deputy Director  
Fred Daniels, Supervisor, Internal Audits, Office of Audit Services, Department of General Services  
Kelly Takigawa, Assistant Division Chief, IT, Policy, Protest and Material Management, Division of Procurement & Contracts  
Rhonda Pile, Office Chief, Commodities & Acquisitions, Division of Procurement & Contracts

BILL FACKENTHALL

CLARK PAULSEN

June 30, 2010

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- c: Joanne Ottens, Office Chief, Policy, Protest, Warehouse, Division of Procurement & Contracts  
Gretchen Brigaman, Acting Branch Chief, Policy, Protests, & Bids, Division of Procurement & Contracts  
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Laurine Bohamera, Chief, Internal Audits, Audits and Investigations  
Kevin Yee, Audit Supervisor, Internal Audits, Audits and Investigations

<b>P4000-375</b>
<b>Department of General Services Contract Delegation Audit</b>
<b>June 2010</b>

**Gerald A. Long**  
**Deputy Director**  
**Audits and Investigations**  
**California Department of Transportation**

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## **Summary**

Audits and Investigations (A&I) has completed the audit required by the Contract Delegation from the Department of General Services (DGS) to the California Department of Transportation (Department). DGS, under Exemption Letter 11.9 (dated June 30, 2008), exempted contracts under \$75,000 from its approval. Under the delegation, the Department is required to maintain an internal control system sufficient to provide reasonable assurance of compliance with State contract laws and procedures. In addition, a biennial audit is required on the internal controls over contracts. This report covers the audit report requirement under the delegation.

The audit focused on contracts processed and executed by the Division of Procurement and Contracts (DPAC). The purpose of the audit was to determine whether internal controls over processing, executing, and managing contracts were adequate and in compliance with State laws, rules, and regulations.

Our audit disclosed that the Department's established policies and internal controls with respect to Contract Delegation are generally adequate, except for the issues noted below:

- Weaknesses over Contract File Documentation
- Untimely Contract Approval
- Weaknesses over Mandatory CAL-Card Training
- Noncompliance - Small Dollar Value Contracts

## **Background**

All State contracts are required to be approved by DGS. According to Government Code 14616, the Director of DGS may exempt any transaction from this legally required approval. The law sets the maximum exemption at \$75,000 and specifies requirements that must be met. The Office of Legal Services (OLS) is responsible for recommending that the Director grant or deny such exemptions after review to ensure that the requirements are met. An internal audit of the process is one of those requirements.

An exemption is granted for a specific period of time and is subject to periodic renewal. The exemption may apply to service contracts and/or consultant service contracts, and may also include other categories of contracts. Also, within these broad categories, certain types of contracts, or contracts awarded by certain methodologies, may also be excluded from the exemption.

On February 2, 1992, DGS granted the Department an exemption by delegating authority to approve service contracts under \$50,000, inter-agency agreements under \$50,000, and hazardous contracts under

\$10,000. The exemption was modified on January 31, 1995, to increase the service contract delegation to \$75,000 per Public Contract Code Section 10351.

DGS renewed the Department's exemption by delegating authority to approve contracts under \$75,000. Exemption letter 11.9, dated June 30, 2008 (supersedes No. 11.8), covers the period from July 1, 2008, through June 30, 2012. The exemption states that two audits are required during the exemption period. The exemption further states that the audits must be conducted in accordance with DGS' Office of Audit Services (OAS) audit guide, and the two audit reports must be submitted to the OAS by June 30, 2010, and by April 30, 2012.

DPAC provides services in the areas of procurement, publications, CAL-Card, property control, warehousing, service contracts, architectural and engineering contracts, and minor public works contracts (under \$117,000).

**Objectives,  
Scope, and  
Methodology**

The purpose of the audit was to determine whether the Department provides reasonable internal controls over processing, executing, and managing contracts in accordance with the DGS exemption, as well as State laws, rules, and regulations. The audit was conducted in accordance with the International Standards for the Professional Practice of Internal Auditing.

The scope of the audit focused on contracts and amendments processed by DPAC from July 1, 2008, through September 30, 2009.

The audit objectives were:

- To determine whether the Department's contracting program is complying with the legal requirements for exemption, and especially oversight of the universe of contracts awarded subject to exemption.
- To document the Department's systems of internal controls over the contracting process.
- To determine whether the Department's contracting system can reasonably be relied upon to provide adequate internal control and produce contracts according to law, State policies, and in the best interest of the State.
- To test the effectiveness of internal controls through evaluation of a sample of contracts awarded during the audit period.
- To determine whether Department management implemented appropriate corrective actions in response to previous audit findings.

**Conclusion**

Our audit disclosed that the Department's established policies and internal controls with respect to Contract Delegation are generally adequate, except for the issues noted below:

- Weaknesses over Contract File Documentation
- Untimely Contract Approval
- Weaknesses over Mandatory CAL-Card Training
- Noncompliance - Small Dollar Value Contracts

**View of  
Responsible  
Official**

We requested and received a response to our findings from the Chief, Division of Procurement and Contracts. This official was in general agreement with the findings and recommendations. Please see Attachment for the complete response.

**ORIGINAL SIGNED BY:**

**GERALD A. LONG**  
**Deputy Director**  
**Audits and Investigations**

**March 5, 2010**  
**(Last Day of Audit Field Work)**

## **FINDINGS AND RECOMMENDATIONS**

### **Finding 1 - Weaknesses over Contract File Documentation**

During our review of a sample of contract files and related documentation, we found the following deficiencies:

- Two of twenty contracts sampled were missing the State Contract Procurement Registration System (SCPRS) number.
- Four contract files could not be located.
- Three claim schedules could not be located.

Failure to register all contracts through the SCPRS and maintaining incomplete contract files violates the Department of General Services (DGS) and California Department of Transportation (Department) policies and procedures. In addition, DGS may withdraw its contract exemption agreement with the Department if weak controls exist over the preparation, execution, and maintenance of contract records.

The DGS Management Memo 03-09 requires State agencies to register any and all purchase documents valued over \$5,000 in the SCPRS system. In addition, State Contracting Manual (SCM) Section 9.09 identifies that each agency is responsible for maintaining all invoices, records, and relevant documentation.

While DPAC is responsible for providing contract management guidance and training, responsibility for contract administration, such as ensuring all contracts are registered in the SCPRS and contract files are properly maintained, overall responsibility lies with the Department's individual contract managers.

### **Recommendation**

We recommend that DPAC remind the Department's contract managers of their contract administration responsibilities through written correspondence and by requiring formal ongoing training.

### **Division of Procurement and Contract's Response**

DPAC concurs with this finding. Management will notify staff of this finding and provide training to the appropriate staff by December 31, 2010. For DPAC's complete response, please see Attachment.

### **Finding 2 - Untimely Contract Approval**

We found that 9 of 20 (45 percent) contracts reviewed were approved after the contract effective date (term start date). Additionally, 1 of 20 (5 percent) of contracts had services rendered before the term start date and 1 of 20 (5 percent) had services performed before contract approval.



**Finding 2 -  
(Continued)**

Late approval and submission for payment, prior to contract approval, can lead to operational inefficiencies. When contracts are not approved timely, delays in startup occur because a contractor cannot officially perform services prior to approval. If a contractor does start work prior to contract approval, the Department cannot pay for services rendered.

The SCM, Vol. 1, Section 4.09(A), revised 10/05, states the basic policy that no contractor should start work until receiving a copy of the formally approved contract. The law provides that when the DGS/OLS approval is required, contracts for services should not begin before receipt of approval or, in the case of an exempt contract, until it is formally approved by the agency.

A similar finding was noted in our prior audit report, dated June 9, 2008 (P4000-372).

While DPAC has responsibility for providing contract management guidance and training, responsibility for contract administration, including payment approval, lies with the Department's individual contract managers.

**Recommendation**

We recommend that:

- DPAC implement procedures to ensure compliance with SCM, Section 4.09(A), Approval and Commencement of Work, and that the contract be executed (have all the required approval signatures and dates) before the start of work.
- DPAC routinely emphasize and reinforce to Department contract managers their contract administration responsibilities of only authorizing work or approving payment for services rendered after the contract is approved.
- The contract analysts evaluate contract start dates when the contract request is received to ensure sufficient processing time is available and, if sufficient time is not available, adjust the contract start date in coordination with the contract requestor.

**Division of  
Procurement and  
Contract's Response**

DPAC will advise staff of this finding and continue monitoring their communication with contract managers to ensure contractors are being advised not to commence work until the contract has been fully approved. Contract analysts will evaluate contract start dates to emphasize and reinforce the importance of complying with the SCM. For DPAC's complete response, please see Attachment.

**Finding 3 -  
Weaknesses over  
Mandatory  
CAL-Card  
Training**

Mandatory CAL-Card training is not always being completed. As of January 2010, we identified 4 of the 5 (80 percent) Cardholders (CH) and 1 of the 5 (20 percent) Approving Officials (AO) in our sample have not completed the CAL-Card training and/or refresher within the last three years.

The lack of training increases the risk of CAL-Card misuse.

CAL-Card Handbook Section 1.13 requires all CAL-Card applicants to complete CAL-Card training prior to becoming either a CH or an AO, and every three years thereafter.

**Recommendation**

We recommend that DPAC's CAL-Card Unit notify CHs and AOs and enforce the Department's CAL-Card training policies/intervention procedures, allowing for suspension or termination of the CAL-Card accounts for those that do not attend a training course within the required three years. Further, any exceptions should be documented in writing, along with a time frame for compliance, and subsequent adherence to the training requirement.

**Division of  
Procurement and  
Contract's Response**

New online training was developed and implemented on May 1, 2010. All CHs and AOs were required to take the new training and submit new applications, ethics certificates, and training certificates by June 1, 2010. This process is 95% complete. CHs and AOs are required to take this training annually, failure to adhere will result in loss of CALCard privileges. For DPAC's complete response, please see Attachment.

**Finding 4 -  
Noncompliance -  
Small Dollar Value  
Contracts**

We reviewed a sample of 20 Service Agreements (ADM-3015) and found that 6 (30 percent) were awarded to the same contractor, in the same location, during the same period and thus were split, circumventing the required competitive bidding level of \$5,000.

Allowing multiple awards for the same service to a single contractor puts the Department at risk for being denied the exemptions from DGS approval, as is currently granted.

State Administrative Manual (SAM), Section 1215 (4.e.), provides that splitting of contracts to avoid any monetary limitations is prohibited. If it is found that more than one contract has been awarded to a single contractor in any one year for work normally considered one undertaking, and the total of the contracts exceeds \$10,000, the agency may be denied the exemptions from DGS approval.

SCM Section 5.03 states that services may not be split to avoid the need to advertise or obtain competitive bids. In particular, a series of related

**Finding 4 - (Continued)** services that would normally be combined and bid as one job cannot be split into separate tasks, steps, phases, locations, or delivery times to avoid adhering to a State law, policy, or departmental procedure.

Lack of DPAC oversight and awareness has contributed to this occurrence.

**Recommendation** We recommend that:

- DPAC ensure compliance with the requirements related to small dollar value contracts/contracts less than \$5,000.
- DPAC ensure that timely reviews and subsequent approval by contract managers are conducted on multiple awards to a single contractor.

**Division of Procurement and Contract's Response** On October 9, 2008, DPAC issued a memorandum requiring ADM 3015s to be reviewed and approved by DPAC. By December 31, 2010, DPAC will review the audit finding with staff and provide training on the competitive bidding process and procedure to ensure compliance with SAM and SCM. For DPAC's complete response, please see Attachment.

**Audit Team** Laurine Bohamera, Chief, Internal Audits  
Kevin Yee, Audit Supervisor  
Laddavanh Southiyanon, Auditor  
Kathy Brooks, Auditor

## **ATTACHMENT**

### **DIVISION OF PROCUREMENT AND CONTRACTS' RESPONSE TO THE DRAFT REPORT**

## Memorandum

*Flex your power!  
Be energy efficient!*

**To:** GERALD A. LONG  
Deputy Director  
Audits and Investigations

**Date:** June 29, 2010

**File:** P4000-375

**ORIGINAL SIGNED BY:**

**From:** WILLIAM FACKENTHALL  
Chief  
Division of Procurement and Contracts

**Subject:** Response to Draft DGS Contract Delegation Audit, (P4000-375)

The Division of Procurement and Contracts (DPAC) has reviewed the draft Contract Delegation Audit Report dated June 9, 2010 covering the audit period of July 1, 2008 through September 30, 2009. Responses have been provided for each finding as follows:

**Finding 1 – Weaknesses over Contract File Documentation**

Audits and Investigations (A&I) reported deficiencies in DPAC's administration of contract files. During the review process, A&I identified the following:

- Two of twenty contracts sampled were missing the State Contract Procurement Registration System (SCPRS) number.
- Four contract files could not be located.
- Three claim schedules could not be located.

**Recommendation:**

A&I recommends that DPAC remind the California Department of Transportation (Caltrans) Contract Managers (CM) of their contract administration responsibilities through written correspondence and by requiring formal ongoing training.

**DPAC Response:**

DPAC concurs with this finding. SCPRS has been replaced with BidSync. Management will notify staff of this finding and provide training to the appropriate staff by December 31, 2010. DPAC's file retention process has been revised by increasing storage capacity, and shortening the on-site storage rotation period to ensure all files are organized and readily accessible.

**Finding 2 – Untimely Contract Approval**

A&I reported 9 of 20 (45 percent) contracts reviewed were approved after the contract effective date (term start date). Additionally, 1 of 20 (5 percent) contracts had services rendered before the term start date and 1 of 20 (5 percent) had services performed before contract approval.

**Recommendation:**

- DPAC implement procedures to ensure compliance with State Contracting Manual (SCM), Section 4.09(A), Approval and Commencement of Work, and that the contract be executed (have all the required approval signatures and dates) before the start of work.
- DPAC routinely emphasize and reinforce to Caltrans CMs their contract administration responsibilities of only authorizing work or approving payment for services rendered after the contract is approved.
- The contract analysts evaluate contract start dates when the contract request is received to ensure sufficient processing time is available and, if sufficient time is not available, adjust the contract start date in coordination with the contract requestor.

**DPAC Response:**

DPAC will advise staff of this finding and continue monitoring their communication with CMs, to ensure contractors are being advised not to commence work until the contract has been fully approved. In conjunction with sending CMs weekly status reports, contract analysts will evaluate contract start dates to emphasize and reinforce the importance of complying with the SCM, Section 4.09(A), Approval and Commencement of Work requirement.

**Finding 3 – Weaknesses over Mandatory CAL-Card Training**

A&I reported that mandatory CAL-Card training is not always being completed. As of January 2010, we identified 4 of the 5 (80 percent) Cardholders (CH) and 1 of the 5 (20 percent) Approving Officials (AO) in our sample have not completed the CAL-Card training and/or refresher within the last three years.

**Recommendation:**

A&I recommends that DPAC's CAL-Card Unit notify CHs and AOs and enforce Caltrans's CAL-Card training policies/intervention procedures, allowing for suspension or termination of the CAL-Card accounts for those that do not attend a training course within the required three years. Further, any exceptions should be documented in writing, along with a time frame for compliance, and subsequent adherence to the training requirement.

**DPAC Response:**

New online training was developed and implemented on May 1, 2010. A hard copy desk reference tool and checklist provides basic step-by-step procedures for use by CHs and AOs. All CHs and AOs were required to take the new training and submit new applications, ethics certificates, and training certificates by June 1, 2010. This process is 95% complete. CHs and AOs are required to take this training annually, failure to adhere will result in loss of CAL-Card privileges.

**Finding 4 – Noncompliance – Small Dollar Value Contracts**

A&I reviewed a sample of 20 Service Agreements (ADM-3015) and found that 6 (30 percent) were awarded to the same contractor, in the same location, during the same period and thus were split, circumventing the required competitive bidding level of \$5,000.

**Recommendation:**

A&I recommends that DPAC ensure:

- Compliance with the requirements related to small dollar value contracts/contracts less than \$5,000.
- Timely reviews and subsequent approval by CMs are conducted on multiple awards to a single contractor.

**DPAC Response:**

On October 9, 2008, DPAC issued a memorandum requiring ADM 3015 be reviewed and approved by DPAC. This requirement has reduced the frequency of circumventing the required competitive bidding process. Additionally, by December 31, 2010, DPAC will review the audit finding with staff and provide training on the competitive bidding process and procedure to ensure compliance with State Administrative Manual, Section 1215 (4.e.), and SCM Section 5.03

If you have any questions or concerns, please contact Kelly Takigawa at (916) 227-6879.

- c: KTakigawa, Assistant Division Chief, IT Acquisitions and Operations  
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